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Hong Kong

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## COMPLY OR EXPLAIN ESG REPORTING FOR HONG KONG LISTED COMPANIES FOR FINANCIAL YEARS STARTING FROM 1 JANUARY 2016

### Introduction

The Stock Exchange of Hong Kong Limited (the **Exchange**) has strengthened listed companies' environmental, social and governance reporting obligations under amendments to the Environmental, Social and Governance Reporting Guide (**ESG Guide**) and related Listing Rules (**Rules**) as proposed in its July 2015 consultation paper.<sup>1</sup>

ESG reporting in accordance with the ESG Guide was previously a recommended practice only. The key change is to upgrade a number of the recommended disclosures under the ESG Guide to "comply or explain" (**comply or explain**). This requires listed companies to report on whether they have complied with the comply or explain provisions of the ESG Guide, and if they have not, they must give considered reasons for their non-compliance.

Most amendments came into effect on 1 January 2016. The "comply or explain" upgrade of the Key Performance Indicators (**KPIs**) in Subject Area A, "Environmental", has however been delayed and will come into effect for issuers' financial years beginning on or after 1 January 2017.

The amendments to the Main Board and GEM Listing Rules are available on the Exchange's website at [http://en-rules.hkex.com.hk/net\\_file\\_store/new\\_rulebooks/m/b/mb\\_esg\\_1601.pdf](http://en-rules.hkex.com.hk/net_file_store/new_rulebooks/m/b/mb_esg_1601.pdf) and [http://en-rules.hkex.com.hk/net\\_file\\_store/new\\_rulebooks/g/e/gem\\_esg\\_1601.pdf](http://en-rules.hkex.com.hk/net_file_store/new_rulebooks/g/e/gem_esg_1601.pdf), respectively. Also

<sup>1</sup> Consultation Paper Review of the Environmental, Social and Governance Reporting Guide, July 2015, available at <https://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp201507.pdf>.

available on the Exchange's website are the revised version of its FAQs on ESG reporting<sup>2</sup> and the Exchange's consultation conclusions.<sup>3</sup>

### Amendments to Main Board Rule 13.91

In the Consultation Conclusions, the Exchange adopted the proposal to amend Main Board Rule 13.91. The amended Main Board Rule 13.91 refers to the ESG Guide in Appendix 27, which now consists of two levels of disclosure obligations: (a) comply or explain provisions; and (b) recommended disclosures.

Listed companies are required to state in either their annual reports or in separate ESG reports whether they have complied with the comply or explain provisions in the ESG Guide. If a listed company has deviated from any of these provisions, it is required to provide considered reasons for doing so. Reporting on the recommended disclosures is voluntary, but is encouraged.

Listed companies are required to disclose ESG information annually, and the information must relate to the same period covered in the annual report. An ESG report may be presented as information in the company's annual report, in a separate report, or on the company's website. If this information is not presented in the company's annual report, the company should publish this information no later than three months after the publication of its annual report.

<sup>2</sup> FAQs – Main Board Listing Rules – Appendix 27.

<sup>3</sup> Consultation Conclusions Review of the Environmental, Social and Governance Reporting Guide, December 2015, available at <https://www.hkex.com.hk/eng/newsconsul/mktconsul/Documents/cp201507cc.PDF>.

The ESG Guide restates these Main Board Rule amendments. The ESG Guide additionally provides that irrespective of the format adopted, the ESG report should be published on the Exchange's website and the listed company's website. For guidance on the comply or explain approach, reference should be made to the "What is comply or explain?" section of the Corporate Governance Code and Corporate Governance Report in Appendix 14 of the Main Board Listing Rules.

## Amendments to the ESG Guide

In the Consultation Conclusions, the Exchange adopted various proposals which amend the ESG Guide in Appendix 27 of the Main Board Rules. The amendments are discussed below.

### A. Revamping the introductory section of the ESG Guide

The introductory section of the ESG Guide has been amended so as to provide additional guidance on reporting and to ensure consistency with international standards. The Reporting Principles (Materiality, Quantitative, Balance (added to the revised ESG Guide) and Consistency) have been reworded.

The revised ESG Guide includes a provision that the Board bears responsibility for evaluating and determining the listed company's ESG-related risks, and ensuring that appropriate and effective ESG risk management and internal control systems are in place. Management is required to provide a confirmation to the board on the effectiveness of these systems.

A section entitled "Complementing ESG discussions in the Business Review Section of the Directors' Report" has been added to the introduction to the ESG Guide. This section is designed to clarify the differing but complementary disclosure requirements under the ESG Guide and the requirement under the new Companies Ordinance (incorporated in Appendix 16 of the Main Board Rules) for a high level discussion of ESG matters in the Business Review Section of the Directors' Report.

### B. Re-arranging the ESG Guide

The ESG Guide has been re-organised into two Subject Areas: A. *Environmental* and B. *Social*. The now former sections of "Workplace Quality", "Operating Practices" and "Community Involvement" have been re-categorised to fall under the new section B. *Social* (with "Workplace Quality" being renamed as "Employment and Labour Practices").

### C. Upgrading the General Disclosures

The General Disclosures under each Aspect of the ESG Guide have been upgraded from recommended (i.e. voluntary disclosure) to comply or explain. Each General Disclosure requires issuers to set out their policies or information on their policies regarding the relevant Aspect. Some General Disclosures additionally require information on compliance with relevant laws and regulations that have a significant impact on the issuer in respect of the relevant Aspect.

The wording of the General Disclosures has been revised in order to be consistent with the directors' reporting requirements under the new Companies Ordinance (Cap. 622 of the Laws of Hong Kong).

### D. Upgrading the KPIs in Subject Area. Environmental

The KPIs in Subject Area A, *Environmental*, have been upgraded from recommended (i.e. voluntary disclosure) to comply or explain. The implementation of this comply or explain upgrade has been delayed, and will come into effect for listed companies' financial years beginning on or after 1 January 2017.

### E. Gender Disclosure

The ESG Guide has been amended to make it consistent with international standards of ESG reporting by including disclosure of gender diversity. The provisions under the sub-heading "Employment and Labour Standards" have been amended to include the following Recommended Disclosures: total workforce by gender; employee turnover rate by gender; the percentage of employees trained by gender; and the average training hours completed per employee by gender.

## Application to GEM

Rule references in the Consultation Conclusions (as well as in this newsletter) apply equally to the equivalent GEM Rules. Thus, GEM Rule 17.103 (equivalent to Main Board Rule 13.91) and the ESG Guide in Appendix 20 of the GEM Rules (equivalent to Appendix 27 of the Main Board Rules) have been similarly amended.

## Implementation Dates

The amendments to the ESG Guide and related Rules will come into effect in two phases.

Effective Date	Amendments	Application
Listed companies' financial years commencing on or after <b>1 January 2016</b>	The Rule amendments and the upgrade of the General Disclosures in the ESG Guide from recommended to comply or explain, and the revised recommended disclosures.	For companies with a financial year commencing 1 January, these amendments will first affect their financial year ending on 31 December 2016.
Listed companies' financial years commencing on or after <b>1 January 2017</b>	The upgrade of the KPIs in Subject Area A, "Environmental", of the ESG Guide from recommended to comply or explain.	For companies with a financial year commencing 1 January, this amendment will first affect their financial year ending on 31 December 2017.

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